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UCLA experts don't buy recession

By Peter Y. Hong

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Brushing aside conventional wisdom, UCLA economists say California and the nation will survive the housing slump and job losses without plunging into recession -- although it will still be miserable for many Americans.

"We are holding firm: no recession this time," UCLA Anderson Forecast Director Edward Leamer said in a report being released today.

Industrial production growth remains strong, the quarterly report notes, and consumer spending on big-ticket items such as refrigerators is expected to keep climbing -- albeit by just 0.3% this year, from 5% at the end of 2007.

Housing remains the big drag on the economy, UCLA analysts say. But they say the rising tide of foreclosures is related more to falling prices and escalating interest rates than to job losses, which triggered previous spikes in foreclosures.

People "are walking away from their homes in droves not because they lost their jobs but because home prices are falling," Leamer said.

Many prominent economists and institutions, including Wall Street powerhouse Goldman Sachs and former Treasury Secretary Lawrence H. Summers, have already declared the economy to be in recession. That is commonly defined as two consecutive quarters of decline in gross domestic product.

UCLA predicts that GDP will dip by 0.4% in the second quarter of this year, but then rebound. Anderson expects GDP to be growing at 2.5% by the end of this year.

In staking out the contrarian position, Leamer noted that UCLA bucked other forecasters in 2001 by correctly predicting that year's recession.

"We got it right, and we stood alone back then," he said. In jest, he added later that he had "submitted my resignation letter, in the event I am wrong."

Whether truly in recession or not, Leamer said the economy would be sputtering. It remains so fragile that "if there is a quick halt to consumer spending, we will for sure have a recession in 2008," he added.

"The question is whether [2008] will be disappointing or horrible; our forecast is disappointing," he said in an interview.

The Anderson forecasters contend that the economy has been wounded mainly by the collapse of residential real estate. The number of jobs overall will continue to increase, but not at a pace fast enough to employ the growing numbers of people seeking work.

National unemployment will peak at 5.6% at the beginning of 2009, according to the forecast, from 4.8% currently.

"In a recession, jobs are easy to lose and hard to find. This time there are not a lot of layoffs, so jobs aren't easy to lose, but they are hard to find," Leamer said.

So far, most of the jobs lost in California and the nation have been in construction and financial services, but those losses are small compared with the severe manufacturing job losses in the recessions of 1990 and 2001.

After the 2001 recession, 358,000 manufacturing jobs were lost in California, UCLA economist Ryan Ratcliff noted. By comparison, the state has shed 55,000 financial sector and 106,000 construction jobs since 2007.

"They're just not the same scope as the previous decline in manufacturing," Ratcliff said.

The Los Angeles area will continue to see job losses more than offset by the addition of new jobs, though the increase in jobs will not keep up with the growing number of job-seekers here.

Still, Los Angeles, Orange County and the San Francisco Bay Area are among the growth areas in the state that UCLA economist Jerry Nickelsburg said "might be growing slower, but they are not running out of gas."

Statewide unemployment will peak at the end of 2008, and will decline slightly in 2009, but will remain close to 6% until 2010 -- when it will fall to 5.5%, UCLA predicts.

Unlike past recessions, the economy will not show dramatic improvements after this period of sluggishness, Leamer predicted.

"In the past 10 years, the U.S. economy has had two locomotives," Leamer said. One was the high-tech stock bubble of the late 1990s, the next was the run-up in housing.

"Looking to the future, there isn't another locomotive. There is still not a reason for great optimism," he said.

Home prices will also be slow to bounce back, and the UCLA forecasters do not predict when the housing market will recover.

Even though the Federal Reserve has cut its benchmark lending rate, mortgage interest rates have not fallen dramatically, said one of the Anderson Forecast authors, David Shulman. "The consumer has yet to benefit from the rate cuts," he said.

It could be months before the accuracy of UCLA's forecast is known. The National Bureau of Economic Research, a private association of leading economists, makes the formal determination of a recession.

The bureau defines recession more broadly than two negative quarters of GDP. It says a recession is "a significant decline in economic activity spread across the economy, lasting more than a few months" evident in GDP, income, employment, production and consumption.

The bureau's Business Cycle Dating Committee typically declares recessions six months to 18 months after the beginning of a downturn. The committee meets irregularly, generally convening when a downturn is clear.

The bureau last determined a recession at the end of 2001, which it said lasted eight months.

UCLA's Anderson Forecast had said in April of that year that there was a 90% chance the economy was in recession**,** an assessment disputed by other economists.

Stanford University economist Robert Hall, who chairs the committee, said in an interview Friday that the measures it used in its decisions "have not declined nearly enough" to declare a recession.

"That's exactly our view," Leamer said.